LIBRARY
SUPREME COURT, U. S.

Office-Supreme Court, U.S.
FILED
AUG 23 1963
JOHN F. DAVIS, CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1963

ESTATE OF EUGENE L. FREELAND, DECEASED, BY SECURITY FIRST NATIONAL BANK, A NATIONAL BANKING ASSOCIATION, EXECUTOR, ET AL.

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,

MITCHELL ROGOVIN,
Assistant Attorney General,

WILLIAM A. FRIEDLANDER,
MARCO S. SONDERSCHEIN,
Attorneys,
Department of Justice,
Washington, D.C. 20530.

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 341

ESTATE OF EUGENE L. FREELAND, DECEASED, BY SECURITY FIRST NATIONAL BANK, A NATIONAL BANKING ASSOCIATION, EXECUTOR, ET AL.

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

The ultimate issue here is whether or not Eugene L. Freeland[1] and Margaret C. Lowthian ("petitioners") are entitled to capital gain treatment on their sales in November 1956 of their respective partner-

[1] Mr. Freeland has died since the transaction here in issue, and his interest is now represented by his estate. His wife, Vera G. Freeland, represented by a conservator, is a party because joint returns were filed for the years in question.

ship interests in the Sam Berger Investment Company (SBIC). Because Section 751(a) of the Internal Revenue Code holds that the gain "attributable to * * * inventory items of the partnership which have appreciated substantially in value" shall be taxed as ordinary income, the Tax Court's decision turned on its finding that the real estate which comprised the partnership's basic asset was being held for sale to customers at the time petitioners sold their interests.[2]

Mr. Freeland, with a 32% interest, was one of two general partners, and Miss Lowthian, Freeland's private secretary in his civil engineering practice, held a limited partnership share of 8% in SBIC. Freeland and one of the clients of his engineering firm, Sam Berger, a real estate developer, formed SBIC to purchase 4500 acres of land near San Diego, California. The total sales price was $4,676,666.66 (computed on the basis of $800 per acre plus interest at 3⅓%), payable $100,000 down and the balance in 20 annual installments. The contract of sale required an escrow of $200,000, to be used for off-site improvements such as bringing water, gas, and other utilities from a distant point. After several unsuccessful attempts to raise the $200,000 escrow money from other sources, Berger's associates in another development corporation agreed to put up the $200,000. In return, these associates received a 20% interest in SBIC. (Pet. App. 5-12.)

---

[2] Sections 751(d)(2)(A) and 1221(1) define "inventory" to include "property held * * * primarily for sale to customers in the ordinary course of" the business.

Shortly after SBIC purchased the land, the Lake Murray Development Company (LMDC), was incorporated for the purpose of subdividing and developing land and constructing homes thereon. The SBIC partners other than petitioners held all the stock of LMDC; Berger was its president. SBIC gave LMDC an option to purchase 500 acres of SBIC's land at $2000 per acre. The option provided, *inter alia*: (1) that LMDC would submit to SBIC all its contracts with subcontractors for all items of work so as to guarantee that the cost would not exceed a certain minimum; and (2) SBIC would be liable for all off-site improvement costs in excess of the $200,000 advanced by LMDC. (Pet. App. 10-12.)

Plans for subdividing 50 acres, as well as a master plan for the entire 4500 acres, were submitted to the San Diego Planning Commission. LMDC exercised part of its option and also began the off-site improvement work for the 500 acre development. A series of disputes between LMDC and SBIC arose and as a result, LMDC and SBIC entered into an amended option agreement covering the 500 acres. The price of the land was changed to $2000 for the first 250 acres and $1800 per acre for all additional acreage. Also, SBIC's guarantee of off-site improvement costs was eliminated. (Pet. App. 14-17.)

LMDC constructed 196 homes, but by the summer of 1955 was in financial difficulties. On May 4, 1956, LMDC became insolvent. Berger was also in financial difficulty and sold his 20% interest in SBIC plus the 10% interests of two trusts of which he, Berger, was trustee to Carlos Tavares and his asso-

ciates (the Tavares group) on August 10, 1956. Tavares then sought to purchase Freeland's share or, in the alternative, have Freeland join his group in the development of the SBIC land. Mr. Freeland decided to sell out, as did Miss Lowthian. On September 7, 1956, they gave the Tavares group an option to purchase their shares and the sale was consummated shortly thereafter. (Pet. App. 18-19.)

The Tax Court rejected petitioners' contention that the partnership had not conducted activities that are the usual indicia of a holding of land for sale to customers, and ruled that SBIC had done these things indirectly through the agency of LMDC. (Pet. App. 21-22.) Therefore, the Tax Court concluded, the land was being held by SBIC primarily for sale to customers in the regular course of business, and sustained the Commissioner's contention that petitioners' gains should be taxed at ordinary income rates. The court of appeals affirmed.

The courts below have properly applied settled principles of law to the particular facts of this case. The record adequately supports the findings adverse to petitioners. There is no conflict of decisions or any other basis for further review.

1. The evidence summarized in the court of appeals' opinion (Pet. App. 23-24) constitutes an adequate foundation for the Tax Court's finding that SBIC originally held the land with the view of subdiving it and selling it to customers in the ordinary course of business, and petitioners do not seriously argue otherwise. Their principle present contention (see Pet. 4) is that the purpose of holding changed

before their sale of their partnership interests, a position that focuses on several events—particularly Berger's sale of his partnership interest. However, as the court of appeals ruled (Pet. App. 25, 30), although there was evidence that could have supported a finding of a change in purpose, the record by no means compelled the Tax Court to rule that petitioners had sustained their burden of demonstrating such a change. To require such a finding on the present record—which shows no more than a failure of the subdivision enterprise and a desire to liquidate it as evidence of a change in purpose—would too readily permit avoidance of the provisions of law that seek to deny capital gains treatment to profits realized upon the sale of inventory. (See Pet. App. 24-26).

2. We recognize (see Pet. 8-9, 16) that the Court of Claims has determined that several other partners of SBIC were entitled to capital gains treatment on their sales of their interests to the Tavares group. See *Morse* v. *United States*, 371 F.2d 474; *Ginsburg* v. *United States*, decided June 14, 1968 (68-1 U.S.T.C. ¶ 9429). Of course, even if those determinations were based on records that are in all respects identical to the evidence in the present case, it would not be grounds for certiorari, since it would only mean that different finders of fact reached different factual conclusions in cases that could have gone either way. Cf. *John Kelley Co.* v. *Commissioner*, 326 U.S. 521.

The records, at all events, are not as alike as petitioners suggest (see Pet. 8-9). The essential difference is that petitioners sold their partnership interests nearly a year before the sales by the partners

involved in the Court of Claims decisions. The Court of Claims found only that the purpose of holding the land had changed by that later date—October 31, 1967—and did not find it necessary to determine exactly when the change had taken place (see Pet. 9). As the Court of Claims said in *Ginsburg* (slip op., p. 5) there is "nothing in *Freeland* essentially at odds with our decisions in *Morse* and the present cases."

3. Petitioners' other contentions (Pet. 10-15) are in substance an attempt to portray the court of appeals opinion as reflecting a conclusion that petitioners had conclusively demonstrated the required change in SBIC's purpose for holding the land. But at most that court, in making such comments as its observation (Pet. App. 24; see Pet. 10) that the Tax Court "might possibly have properly found in petitioners' favor", was indicating a view that the basic factual question at issue here could have been decided for either side, and that whatever the decision of the finder of fact, the court of appeals would have affirmed. The fact that the evidence could be given another construction or that the evidence would support a conclusion either way does not, as petitioners seem to argue, make the Tax Court's findings clearly erroneous. Petitioners' burden is to show that the evidence cannot support the findings actually made, *United States* v. *Real Estate Boards*, 339 U.S. 485, 495-496; *United States* v. *Yellow Cab Co.*, 338 U.S. 338, 342—something they cannot do.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

MITCHELL ROGOVIN,
Assistant Attorney General.

WILLIAM A. FRIEDLANDER,
MARCO S. SONNENSCHEIN,
Attorneys.

AUGUST 1968.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1968 317291 128